83-1996

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IN THE

Supreme Court of the United States

1983 TERM

FEDERAL DEPOSIT INSURANCE CORPORATION,
Plaintiff-Respondent,

vs.

THE MERCHANTS NATIONAL BANK OF MOBILE,
Defendant-Petitioner.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

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QUESTIONS PRESENTED

1. Whether 12 U.S.C. § 1823(e) which renders certain unrecorded agreements unenforceable against FDIC, can be invoked to preclude evidence, otherwise admissible, of disputed terms of an ambiguous asset in the absence of any collateral agreement.

2. Whether FDIC is equitably estopped to assert that the loan participation agreement received the benefit of an FmHA guarantee when FDIC not only had actual knowledge of the fact that the loan participation was without benefit of the FmHA guarantee, but indeed approved such participation.

CERTIFICATE OF INTERESTED PERSONS

The undersigned, counsel of record for Petitioner, The Merchants National Bank of Mobile, certify that the following list of persons are interested persons within the meaning of Rule 28.1 of the Rules of the Supreme Court of the United States:

1. The Merchants National Bank of Mobile

2. Federal Deposit Insurance Corporation

3. First Alabama BancShares, Inc., holding company of The Merchants National Bank of Mobile, and its affiliates:

The Merchants National Bank of Mobile
First Alabama Bank of Montgomery, N.A.
First Alabama Bank of Birmingham
First Alabama Bank of Huntsville, N.A.
First Alabama Bank of Tuscaloosa, N.A.

First Alabama Bank of Dothan
First Alabama Bank of Anniston, N.A.
First Alabama Bank of Selma, N.A.
First Alabama Bank of Athens, N.A.
First Alabama Bank of Troy, N.A.
First Alabama Bank of Talledega County, N.A.
First Alabama Bank of South Baldwin
First Alabama Bank of Gadsden, N.A.
First Alabama Bank of Lauderdale County
First Alabama Bank of Hartselle
First Alabama Bank of Guntersville
First Alabama Bank of Conecuh County
First Alabama Bank of Sumter County
First Alabama Bank of Cullman
First Alabama Bank of Baldwin County, N.A.
First Alabama Bank of Phenix City, N.A.
First Alabama Bank of Chilton County
First Alabama Bank of Walker County
First Alabama Bank of Lee County, N.A.
First Alabama Real Estate Financing, Inc.
First Alabama Leasing, Inc.
First Alabama Investment Counselors, Inc.

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OPINIONS BELOW

The decision of the United States Court of Appeals for the Eleventh Circuit is reported at 725 F.2d 634 and is reprinted in the Appendix. The opinion of the United States District Court for the Southern District of Alabama has not been reported, but is reprinted in the Appendix.

JURISDICTION

The judgment and opinion of the United States Court of Appeals for the Eleventh Circuit was entered on February 24, 1984. Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The pertinent part of 12 U.S.C. § 1823(e), as amended, provides:

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said Board or Committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

STATEMENT OF THE CASE

This case was commenced on February 20, 1981 when Plaintiff-Respondent, Federal Deposit Insurance Corporation (hereinafter "FDIC"), filed its complaint against Defendant-Petitioner, The Merchants National Bank of Mobile (hereinafter "MNB") in the United States District Court for the Southern District of Alabama, Southern Division, alleging jurisdiction under 28

U.S.C. § 1345 and 12 U.S.C. § 1819(4). The complaint alleged that on March 7, 1978, FDIC in its general corporate capacity purchased certain assets formally owned by Wilcox County Bank (hereinafter "WCB"), including a Certificate of Participation in a loan from MNB to Ball-Co Contractors, Inc. (hereinafter "Ball-Co") dated September 1, 1977.[1] The complaint

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[1]The Ball-Co loan was in the amount of $3.9 million and was secured by a mortgage, security agreements and pledges. In addition, FmHA guaranteed the repayment of eighty (80%) percent of the loan amount. As part and parcel of the loan closing, the eighty (80%) percent guaranteed portion of the loan was sold on the secondary money market to Eastern Airlines Pension Fund, and participations in the remaining twenty (20%) percent unguaranteed portion of the loan were sold to several local lending institutions, including WCB, with MNB retaining the largest share of the unguaranteed portion. The Certificate of Participation issued to and accepted by WCB describes the mortgage, security agreements and pledges as collateral, but it makes no mention of the FmHA guarantee.

further alleged that payment of eighty (80%) percent of the participation was guaranteed by the Farmers Home Administration (hereinafter "FmHA") and that it was so entered on the books and records of WCB, and that MNB failed to share the benefits of that guarantee on a pro rata basis with WCB.

MNB's answer, as amended, admitted that WCB had participated in the Ball-Co loan, but denied that WCB participated in the FmHA guaranteed portion of said loan, and averred that FDIC had received all of WCB's pro rata share of collections.

Trial of the action was held before the Court on September 21, 1982. FDIC put forth only one witness, Mr. Herbert Adkison of the FDIC, liquidator of WCB, who testified to the purchase of the loan participation from WCB, and to specific,

and ambiguous, records concerning the loan participation in the files of WCB.[2] He did not testify, nor was there any evidence, as to any alleged collateral agreement between WCB and MNB.

MNB was not permitted to cross-examine Mr. Adkison concerning the ambiguous WCB records, nor was it permitted to introduce evidence that FDIC had actual knowledge of the participation which was contrary to their arguments advanced in court. Further, the trial judge so construed § 1823(e) that he would not receive any evidence offered by MNB proving that the asset did not contain the FmHA guarantee,

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[2]There were no FmHA guarantee documents included in the WCB files, only the documents specifically related to the security for the loan participation.

but he allowed MNB to make an offer of proof.[3]

On October 1, 1982, the Court held that FDIC was entitled to the benefits of the FmHA guarantee[4] and entered its opinion, order and judgment in favor of FDIC in the amount of $67,200.00 with interest in the sum of $20,491.40, and taxed costs to

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[3]MNB's offer of proof essentially set forth: (1) that MNB at no time entered into any collateral agreement with WCB; (2) that WCB and its Chairman knew that the loan participation was unguaranteed; (3) that MNB did not forward to WCB any of the FmHA guarantee documents with the Certificate of Participation; (4) that FDIC, its Regional Director and two (2) field examiners knew that WCB participated in the unguaranteed portion of the loan; (5) that an FDIC Deputy Director approved that very unguaranteed loan participation.

[4]There was no evidence that MNB received any payment under the FmHA guarantee. To the contrary, all proceeds of the FmHA guarantee were paid directly to the Eastern Airlines Pension Fund.

Petitioner. The District Court found (1) that the minutes[5] of the Loan Committee of WCB declared the Certificate of Participation to have the benefit of the FmHA guarantee, regardless of the fact that the Certificate itself did not mention the

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[5]The minutes, dated twelve (12) days after the Certificate of Participation, state:

> A participation loan previously approved by the Loan Committee Members Jim Branum and Joe Williams was ratified. This loan for $84,000.00 participating with the Merchants National Bank of Mobile on Ball-Co Contractors, Inc., which has an 80% F.H.A. [FmHA] guarantee on an original loan of $3,900,000.00. This loan secured by equipment, inventory and real estate. [Emphasis added].

On this basis, the District Court found MNB liable.

FmHA guarantee,[6] and (2) that, pursuant to § 1823(e), FDIC was entitled to judgment against MNB based on the description of the asset contained in those minutes, regardless of the fact that MNB was not privy to those minutes and did not assert as a defense any collateral agreement.

Petitioner appealed to the United States Court of Appeals for the Eleventh Circuit, which affirmed the judgment of the trial court. It held as follows:

1. MNB's Theory. MNB contended that before invoking § 1823(e), a determination

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[6]Also, MNB proffered evidence that the Chairman of the Board of WCB, who handled the transaction, knew that those ambiguous minutes, as so interpreted, did not set forth the true and correct fact that WCB did not participate in the FmHA guarantee.

had to be made as to what the asset was before any determination could be made as to whether an alleged collateral agreement diminished FDIC's interest in the asset. The Eleventh Circuit extended the reach of § 1823(e) to become an evidentiary statute by holding that it precluded evidence, otherwise admissible, to determine the contractual dispute as to the terms of the Certificate of Participation. The Eleventh Circuit stated with respect to the cases[7] cited by MNB that § 1823(e) did not apply, that "in such cases the parties contend that no asset exists or an asset is invalid and that such invalidity is caused by acts

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[7]Howell v. Continental Credit Corp., 655 F.2d 743 (7th Cir. 1981); Riverside Park Realty Co. v. FDIC, 465 F. Supp. 305 (N.D.Tenn. 1978).

independent of any understanding or side agreement." 725 F.2d at 639. The Court thus failed to correctly apply controlling case law as MNB never advanced any collateral agreement as its defense. Admissible evidence would have shown that no FmHA guarantee existed with respect to the Certificate of Participation purchased by WCB. Accordingly, § 1823(e) was incorrectly construed to preclude evidence of the intent of the parties and the terms of the Certificate of Participation itself.

2. Knowledge of FDIC. MNB further contended that knowledge by FDIC that its predecessor in interest, WCB, did in fact participate in the unguaranteed portion of the Ball-Co loan was relevant both to determine whether WCB did so participate and to prove equitable estoppel against

FDIC. The Eleventh Circuit held that FDIC's knowledge was irrelevant under either inquiry because such knowledge constituted notice of a "side agreement" not meeting the requirements of § 1823(e). Again, there was no evidence of any collateral or side agreement between the parties, and MNB has not sought to enforce any such collateral agreement. Yet, the Eleventh Circuit quoted public policy reasons for its determination that FDIC should not be liable for its knowledge of the true and correct terms of the asset.[8]

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[8]The Court's holding emasculates its own approval of Gunter v. Hutcheson, 492 F. Supp. 546 (N.D. Ga. 1980), affirmed 674 F.2d 862 (11th Cir. 1982) that "the FDIC must be governed by a uniform rule that it must be on guard only against . . . actual knowledge at the time the purchase and assumption transaction begins." 492 F. Supp. at 555. See also Gilman v. FDIC, 660 F.2d 688 (6th Cir. 1981).

REASONS FOR GRANTING THE WRIT

I.

THE CASE PRESENTS TWO (2) IMPORTANT QUESTIONS OF FEDERAL LAW WHICH SHOULD BE SETTLED BY THIS COURT.

Petitioner is the first entity in recorded case law construing § 1823(e) to have been barred from presenting evidence as to the terms of an asset. The rationale of the Court of Appeals that § 1823(e) is applicable as an evidentiary statute to prevent introduction of evidence concerning the terms of the asset in question, without regard as to whether any collateral agreement is advanced, is untenable under the existing case law and constitutes an unwarranted expansion of the statute beyond Congressional intent.

The cases construing § 1823(e), and cited by FDIC in its brief on appeal, all

show a common factual theme, to-wit: a readily identifiable asset purchased by the FDIC from an insolvent financial institution and an attempt by the obligor to alter the written terms of that asset by enforcing the terms of a collateral agreement.[9]

However, in the present case, MNB has not attempted to assert any collateral agreement and no evidence of any alleged

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[9]FDIC has relied on Black v. FDIC, 640 F.2d 699 (5th Cir. 1981) (breach of alleged collateral agreement to provide additional construction financing); FDIC v. Hoover-Morris Enterprises, 642 F.2d 785 (5th Cir. 1981) (alleged breach of collateral agreement not to seek deficiency judgment); Chatham Ventures, Inc. v. FDIC, 651 F.2d 355 (5th Cir. 1981) (breach of alleged oral joint venture agreement); FDIC v. Latimore Land Corporation, 656 F.2d 139 (5th Cir. 1981) (breach of collateral agreement to provide additional necessary financing).

agreement has ever been identified or introduced into evidence by FDIC or MNB. The issue involved is what the terms of the asset are, not that a readily identifiable asset is being diminished by a collateral agreement.[10]

The terms of the statute specifically render unenforceable collateral agreements, and only such agreements, by and between the obligor and obligee. Without any such collateral agreement, the statute is inapplicable. Howell v. Continental Credit Corp., 655 F.2d 743 (7th Cir. 1981); Riverside Park Realty Co. v. FDIC, 465 F. Supp. 305 (M.D. Tenn. 1978).

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[10]This distinction can be addressed as the difference between an "asset" case and an "agreement" case for purposes of § 1823(e). The statute is applicable to the latter, but not the former.

The decision of the Court below, so long as it stands unreversed, constitutes a serious threat to national banking policy, as set forth by Congress, by granting FDIC the ability to define an asset purchased from an insolvent financial institution in any manner it arguably sees fit without regard to the totality of evidence which defines the terms of that asset.

Furthermore, the Eleventh Circuit decided that public policy dictated "against holding FDIC liable for its knowledge" of the terms of an asset. This rationale carves an untenable exception into the doctrine of equitable estoppel by allowing FDIC to disregard not only its knowledge of the facts in issue, but also the approval of its Deputy Director that the very loan participation agreement made the subject of this litigation could be

entered into. Indeed, it was FDIC's approval of the transaction which induced MNB to become the lead bank.[11]

This broad exception to the doctrine of equitable estoppel[12] clearly threatens to

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[11]MNB was not originally scheduled to be the lead bank in the Ball-Co loan. MNB proferred evidence that five (5) days before the loan closed, the originally scheduled lead bank, First National Bank of Fairhope (FNBF) discovered it could not so act. FNBF joined with FmHA in asking MNB to assume the lead bank position. MNB agreed to do so provided that WCB and the other loan participants adhered to their unguaranteed participations. To verify that WCB could participate in the unguaranteed portion of the loan, MNB called a Deputy Director of FDIC who stated that such participation by WCB was indeed permissible and approved.

[12]The fundamental principles of equitable estoppel apply to governmental agencies as well as private parties. This doctrine is set forth in Investors Research Corp. v. Securities and Exchange Commission, 628 F.2d 168 (D.C. Cir. 1980), cert denied, 449 U.S. 919, 66 L.Ed.2d 146 (1980); Michigan Wisconsin Pipeline Co. v.

make the FDIC immune from defenses based on the terms of an asset itself, and serves to severely hamper the dealings of national banks with each other, whether intra-state or interstate, as well as with the FDIC.

II.

THE DECISION BELOW IS IN CONFLICT WITH THE DECISIONS OF OTHER COURTS OF APPEAL ON THE SAME MATTER.

The Court of Appeals for the Seventh Circuit, in Howell v. Continental Credit Corp., 655 F.2d 743 (7th Cir. 1981), has found that in the absence of an alleged collateral agreement, § 1823(e) is

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(footnote 12 continued)

Williams-McWilliams Co., 551 F.2d 945 (5th Cir. 1977); The Merchants National Bank of Mobile v. United States, 689 F.2d 181 (Ct.Cl. 1982); TRW, Inc. v. F.T.C., 647 F.2d 942 (9th Cir. 1981); Emeco Industries, Inc. v. United States, 485 F.2d 652 (Ct.Cl. 1973).

inapplicable. Furthermore, the Eleventh Circuit, in Gunter v. Hutcheson, supra, concluded that in the absence of a collateral agreement, § 1823(e) does not operate to bar fraud claims. There is no viable distinction between the right of an obligor to assert fraudulent inducement as a defense and the right of an obligor to present the totality of evidence which defines the terms of the asset in question, where the nature of the asset is genuinely disputed.

Indeed, the reported cases on § 1823(e) from each appellate circuit[13] conflict

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[13] See, e.g., FDIC v. deJesus Velez, 678 F.2d 371 (1st Cir. 1982); FDIC v. Waldron, 630 F.2d 239 (4th Cir. 1980); Chatham Ventures, Inc. v. FDIC, 651 F.2d 355 (5th Cir. 1981), cert. denied, 456 U.S. 972, 102 S.Ct. 2234, 72 L.Ed.2d 845 (1981); FDIC v. Rosenthal, 477 F. Supp. 1223 (E.D. Wis. 1979), affirmed, 631 F.2d 733 (7th Cir. 1980); Howell v. Continental Credit Corp., supra (7th Cir. 1981); Gunter v. Hutcheson, supra (11th Cir. 1982).

with the holding of the Court below in that, without exception, a collateral agreement was sought to be enforced and was declared unenforceable as required by the statute.

CONCLUSION

For these reasons, a writ of certiorari should be issued to review the judgment and opinion of the United States Court of Appeals for the Eleventh Circuit.

Respectfully submitted,

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205/432-7682

Attorneys for Petitioner

CERTIFICATE OF SERVICE

I do hereby certify that I have on this 4th day of June, 1984 served three (3) copies of the foregoing on Joseph B. Mays, Jr., Counsel for Respondent and three (3) copies on the Solicitor General by mailing the same by United States mail, properly addressed and first-class postage prepaid, all in accordance with Rules 28.3 and 28.4 of the Rules of the Supreme Court of the United States.

Alan C. Christian

APPENDIX

IN THE UNITED STATES DISTRICT COURT FOR
THE SOUTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

FEDERAL DEPOSIT INSURANCE CORPORATION,	)	
Plaintiff,	)	CIVIL ACTION
vs.	)	NO. 81-0124-P
THE MERCHANTS NATIONAL BANK OF MOBILE,	)	
Defendant.	)	

OPINION AND ORDER

The plaintiff, Federal Deposit Insurance Corporation (FDIC), brought this action in its general corporate capacity as liquidator of the Wilcox County Bank (WCB) of Camden, Alabama against the defendant, Merchants National Bank (MNB) of Mobile, Alabama, claiming the benefit of a Farmers Home Administration (FmHA) guarantee covering 80% of $3.9 million loan to Ball-Co Contractors, Inc. (Ball-Co), for

which MNB was the lead bank, and in which WCB held an $84,000 participation. The matter came to trial on September 21, 1982. Upon consideration of the record, evidence, and arguments of counsel, the court enters the following Opinion and Order.

Findings of Fact

Plaintiff is a federally chartered corporation created and existing by virtue of the Federal Deposit Insurance Act, 12 U.S.C. §§ 1811-1832 (1976).

Defendant is a national banking association with its principal offices at 106 St. Francis Street, Mobile, Alabama.

Jurisdiction of this court is proper under 28 U.S.C. § 1345 (1976) and 12 U.S.C. § 1819(4) (1976).

WCB was formerly a state banking association chartered pursuant to the laws of the State of Alabama.

On March 1, 1978, the Alabama State Superintendent of Banks declared WCB to be insolvent. On March 1, 1978, the Alabama State Superintendent of Banks appointed the FDIC as Receiver of WCB pursuant to 12 U.S.C. § 1821(c) (1976). The FDIC accepted the appointment.

By order entered March 7, 1978, in proceedings styled In the Matter of the Liquidation of Wilcox County Bank, Camden, Alabama, Civil Action No. 78 CV-12, the Circuit Court of Wilcox County, Alabama ratified the appointment of the FDIC as Receiver of WCB and authorized and approved the sale by FDIC, as Receiver, of certain assets of WCB to FDIC, in its general corporate capacity.

The aforesaid agreement of sale between the FDIC, as Receiver of WCB, and the FDIC, in its general corporate capacity, vested the FDIC in its general corporate capacity with all right, title and interest in and to certain assets of the former WCB, including WCB's $84,000 loan participation with MNB, as lead bank, in the $3,900,000 loan by MNB to Ball-Co, which loan was 80% guaranteed by the FmHA. The loan participation of WCB is an asset of the FDIC.

The minutes of the meeting of the loan committee of WCB, held on September 12, 1977, show that the subject asset included a participation in the guaranteed portion of the loan. Those minutes read as follows:

> A participation loan previously approved by the Loan Committee Members Jim Branum and Joe Williams was ratified. This loan

for $84,000 participating with the Merchants National Bank of Mobile on Ball-Co Contractors, Inc., which has an 80% FHA guarantee on an original loan of $3,900,000. This loan secured by equipment inventory and real estate. This loan is considered a credit worthy loan, however, it was approved only after being advised by the Merchants National Bank of Mobile that the loan sufficient to reduce personal loans held by the bank on Lowell Harrelson would be placed in jeopardy if we did not participate. Our loans to Mr. Harrelson including the loan charged off amount of $78,450.46 and an additional loan of $38,700.00, which we had previously sold to our principal correspondent, Southern National Bank. The advantage we gained from getting these loans paid in full certainly justifies our participation in a loan for approximately the same amount, which has an 80% FHA guarantee. We have been assured by the participating bank that funds have been provided in the advance on the new loan to retire Mr. Harrelson's personal debts and we have, also, been assured by Mr. Harrelson that these loans will be taken out soon.

At the time FDIC purchased the said loan participation, there was no agreement

in any of WCB's records which tended to diminish of defeat the FDIC's right, title or interest in such asset as a guaranteed loan, and there was no such agreement which met the requirements of 12 U.S.C. § 1823(e), i.e., which was: (1) in writing; (2) executed by WCB and MNB contemporaneously with the acquisition of said asset by WCB; (3) approved by the board of directors of WCB or its loan committee, which approval was reflected in minutes of said board or committee. No such diminishing agreement has ever been in any official record of WCB.

MNB received the principal sum of $3,120,000.00 on September 1, 1977 for 80% of the $3.9 million Ball-Co loan. No part of the said $3,120,000.00 was distributed either to WCB or to the FDIC.

Conclusions of Law

The FDIC acquired the WCB loan participation, which is the subject of this lawsuit, in the course of a purchase and assumption transaction entered into pursuant to 12 U.S.C. § 1823(e).

The second paragraph of 12 U.S.C. § 1823(e) provides:

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

The Congressional intent behind the second paragraph of Section 1823(e) was to protect the FDIC from agreements not reflected in the bank records that tend to diminish in any way the rights of the FDIC in assets acquired pursuant to Section 1823(e), first paragraph.

In the present case, the documents in the possession of WCB at the time the FDIC purchased the asset in question reflected that said asset was 80% guaranteed by FmHA. Nothing in the books and records of WCB indicates or suggests that the participation is other than 80% guaranteed by FmHA.

Under the provisions of the second paragraph of 12 U.S.C. § 1823(e), the FDIC, as purchaser of this asset under a purchase and assumption transaction, is entitled to rely upon the records of WCB with respect

to the asset. Inasmuch as those records show the loan to be 80% guaranteed by FmHA, the FDIC is entitled to the benefit of those guarantees.

Accordingly, the court concludes that plaintiff is entitled to judgment in its favor.

It is therefore ORDERED, ADJUDGED and DECREED that judgment be and is hereby entered in favor of the plaintiff, Federal Deposit Insurance Corporation, and against the defendant, The Merchants National Bank of Mobile, in the amount of $67,200.00, together with interest as provided for by Ala. Code § 8-8-1 as last amended, to wit: $20,491.40, totaling $87,691.40.

Costs are taxed against the defendant.

DONE at Mobile, Alabama, this the 1st day of October, 1982.

s/Virgil Pittman
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT FOR
THE SOUTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

FEDERAL DEPOSIT INSURANCE CORPORATION, Plaintiff, vs. THE MERCHANTS NATIONAL BANK OF MOBILE, Defendant.	)	CIVIL ACTION NO. 81-0124-P

Appeal from the United States District Court for the Southern District of Alabama.

Before GODBOLD, Chief Judge, RONEY and SMITH,* Circuit Judges.

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*Honorable Edward S. Smith, U.S. Circuit Judge for the Federal Circuit, sitting by designation.

GODBOLD, Chief Judge:

I. Introduction

By 12 U.S.C. Sec. 1823(e) (1976) Congress gave to assets acquired by the Federal Deposit Insurance Corporation special protections that are not available to ordinary holders of commercial paper and are not dependent on whether FDIC would qualify as a holder in due course under state law. This case concerns application of Sec. 1823(e) to an asset acquired by FDIC from a failed bank. Section 1823(e) provides:

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the

> acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

Merchants National Bank (MNB) held 80% of $3.9 million loan to Ball-Co Contractors, Inc. Wilcox County Bank (WCB), along with other banks, participated in the remaining 20% of the loan. WCB's share was $84,000. The $3.9 million Ball-Co loan carried an 80% guarantee from the Farmers Home Administration. WCB says that it participated ratably in the guaranteed portion. MNB says that WCB participated in only the unguaranteed portion.

The certificate of participation issued by MNB to WCB says:

To: WILCOX COUNTY BANK

This is to certify that you have a participation of $84,000.00 EIGHTY FOUR THOUSAND & NO/100 DOLLARS in the following described loan held by the undersigned:

BORROWER: BALL-CO CONTRACTORS, INC.

ADDRESS: P. O. Box 880
Bay Minette, AL

AMOUNT OF NOTE: $3,900,000.00

DATED: August 31, 1977 DUE:_____

INTEREST RATE: 3% over Prime
INTEREST TO YOU: Same

COLLATERAL: All accounts receivable and contract rights of Debtor, all of Debtor's inventory, including all raw materials, work in process, finished goods and other tangible property owned and held for sale or lease or furnished under contracts of service or used or consumed in Debtor's business, all equipment used in the conduct of the business of Debtor; and all motor vehicles and automotive equipment used in the conduct of the business of Debtor now owned or hereafter existing or acquired.

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The Merchants National Bank of Mobile shall be entitled to hold the note or other evidence of debt together with all collateral or security thereto, and to share in same on a pro rata basis with the holder hereof, and to exercise its discretion in collecting the same and selling any security therefor. The said Merchants National Bank of Mobile shall be free from any liability to the holder hereof except for its proportionate share of collections of principal and interest when received. It is agreed that any attorneys' fees or collection charges incurred will be shared on a pro rata basis by the participating banks.

The MNB/Ball-Co loan agreement delivered to WCB with the certificate indicates that the loan is protected by an 80% FmHA guarantee.

The minutes of WCB directors' meetings say:

> A participation loan previously approved by the Loan Committee Members Jim Branum and Joe Williams was ratified. <u>This loan for $84,000 participating with the Merchants National Bank of Mobile on Ball-Co Contractors, Inc.,</u>

> which has an 80% FHA guarantee on an original loan of $3,900,000. This loan is considered a credit worthy loan, however, it was approved only after being advised by the Merchants National Bank of Mobile that the loan sufficient to reduce personal loans held by the bank on Lowell Harrelson would be placed in jeopardy if we did not participate. Our loans to Mr. Harrelson including the loan charged off amount of $78,450.46 and an additional loan of $38,700.00, which we had previously sold to our principal correspondent, Southern National Bank. The advantage we gained from getting these loans paid in full certainly justifies our participation in a loan for approximately the same amount, which has an 80% FHA guarantee. We have been assured by the participating bank that funds have been provided in the advance on the new loan to retire Mr. Harrelson's personal debts and we have, also, been assured by Mr. Harrelson that these loans will be taken out soon.

(emphasis added).

MNB sold its 80% participation in the loan to Eastern Airlines Pension Fund. Ball-Co defaulted on its obligations under

the note and loan agreement, Eastern called on FmHA to honor its guarantee, and FmHA paid Eastern an amount equal to 80% of the value of the loan.

WCB, of Camden, Alabama, was formerly a state banking association chartered under the laws of Alabama. The Alabama superintendent of banks declared WCB insolvent and appointed FDIC as receiver pursuant to 12 U.S.C. Sec. 1821(e) (1976). FDIC, as receiver, executed an agreement of sale with FDIC in its general corporate capacity. This agreement vested FDIC in its general corporate capacity with all right, title and interest in and to certain assets of WCB, including the $84,000 loan participation.

WCB received none of the proceeds from the MNB-Eastern sale and none of the payment by FmHA to Eastern on the

guarantee. FDIC in its general corporate capacity sued MNB and alleged that FDIC was entitled to participate in the guaranteed portion of the loan. Specifically, FDIC alleged breach of fiduciary duty, breach of contract, and negligence by MNB because of its failure to remit to FDIC its share of MNB's "collection" on the 80% guaranteed portion of the loan that MNB sold to Eastern and FmHA subsequently paid when Ball-Co defaulted. FDIC's pleadings could also be construed, though less clearly, to allege breach of contract, breach of fiduciary duty, and negligence by MNB in the sale of WCB's participation in the 80% guaranteed portion to Eastern (taking at face value FDIC's contention that its asset was participation in the guaranteed portion) without WCB's consent and without remitting to WCB its portion of the proceeds of the sale.

MNB took the position that WCB had participated in only the unguaranteed portion of the Ball-Co loan. FDIC maintains that the books and records of the bank showed that WCB participated ratably in the guaranteed portion and that under Sec. 1823(e) FDIC, as holder of the participation, had the right to share in the proceeds of the guarantee on a pro rata basis. MNB asserted that FDIC, by its alleged knowledge of WCB's participation in the unguaranteed portion, was equitably estopped from relying on the books and records of the bank and that extrinsic evidence, such as intent of the parties, knowledge by FDIC, and surrounding circumstances, showed that WCB's participation was in the unguaranteed portion of the loan.

In determining whether WCB's participation was in the guaranteed or unguaranteed portion the district court correctly applied Sec. 1823(e) to exclude as irrelevant any evidence not found in the records of the bank and not meeting the statute's strict requirements. After a bench trial the district court correctly found that WCB participated in the guaranteed portion of the Ball-Co loan and accordingly entered judgment for FDIC for $87,691.40 (representing 80% of WCB's $84,000 participation plus $20,491.40 in interest). We affirm.

II. Section 1823(e) and the finding of the district court

A. FDIC's purchase and assumption alternative.

We recently discussed the alternatives available to FDIC in discharging its duties when an insured bank fails. See Gunter v.

Hutcheson, 674 F.2d 862, 865-66 (11th Cir.), cert. denied, _____ U.S. _____, 103 S.Ct. 60, 74 L.Ed.2d 63 (1982). When an insured bank fails, FDIC can make direct deposit insurance payoffs on insured deposits. The bank remains permanently closed, and all insured accounts are paid off to the insured limit. The direct payoff alternative is not the preferred one:

> The undesirability of the deposit insurance payoff alternative is readily apparent. A bank failure and a subsequent payoff of insured deposits results in an interruption of vital banking services to the community which the failed bank served. The failed bank's main office and any branches which it operated are permanently closed. As a consequence, virtually all of the failed bank's employees are without jobs. All time, demand and saving deposit accounts of the failed bank are frozen and any checks in transit at the time the bank closed are returned unpaid to the drawer. Furthermore, any depositor of the failed bank with

a deposit account that exceeded the $40,000 statutory insurance limitations (and any other creditor with provable claims) must await the payment of ratable dividends to recover the uninsured portion of his or her deposits. Even those depositors whose accounts are fully insured suffer some hardship since the FDIC ordinarily requires several days in which to reconcile accounts and prepare deposit insurance checks. Finally, any going concern value that the failed bank may have had as a viable banking enterprise is lost irrevocably with the permanent closing of its business. As a consequence of the foregoing, the FDIC is concerned that a deposit insurance payoff in connection with the failure of a bank, particularly a sizable bank, may cause an erosion in public confidence in other banks in the community. Clearly, the failure of a sizeable bank may affect affiliated banks as well as independent banks over a wide geographic area, depending upon the extent of interbank relationships in which the failed bank was involved.

Burgee, Purchase and Assumption Transactions Under the Federal Deposit Insurance Act, 14 The Forum 1146, 1153

(1979) (senior counsel in office of general counsel of FDIC explains FDIC's options).

On the other hand, FDIC can undertake a purchase and assumption transaction when the insured bank fails. FDIC as receiver of the failed bank sells acceptable assets of the failed bank to another financially sound and insured bank (the assuming bank). In return the assuming bank assumes all the failed bank's deposit liabilities. FDIC as receiver obtains full value for the acceptable assets as well as a premium from the assuming bank for the "going concern" value of the failed bank. The value of the assets purchased by an assuming bank plus the premium it pays is always less than the amount of liabilities (such as deposits) that it assumes. To generate cash that can be transferred to the assuming bank to balance the value of the assets and

liabilities it assumes, FDIC as receiver contracts with FDIC in its corporate capacity to purchase the assets that are unacceptable to the assuming bank. This purchase was authorized by 12 U.S.C. Sec. 1823(e) (1976) and following the Depository Insurance Flexibility Act, Pub.L. No. 97-320, 96 Stat. 1469 (1982), is now authorized by 12 U.S.C. Sec. 1823(c) (1982). Thus FDIC in its corporate capacity pays FDIC as receiver an amount equal to the cash difference between the value of the assets purchased and liabilities assumed by the assuming bank, less the amount of the premium paid by the assuming bank. See generally id. at 1154-55.

The purchase and assumption transaction has several advantages for FDIC and the public:

> The Purchase and Assumption transaction avoids the numerous adverse results of the deposit insurance payout method. Virtually all of the failed bank's depositors and other creditors are fully protected by the assumption of their deposits and debts by the assuming bank. The FDIC as insurer of deposits is relieved from the difficult and time consuming obligation of paying off hundreds or even thousands of depositors. Of utmost significance is the fact that the banking services to the citizens of the community previously served by the failed bank continue uninterrupted as the assuming bank agrees to reopen all of the failed bank's offices on the next business day. Of particular significance is the fact that the receiver obtains the benefit of a premium, which is often substantial, for the going concern value of the failed bank that would be lost in the event of a deposit payoff.

Id. at 1156.

Although FDIC favors the use of the purchase and assumption alternative, it does not have unbridled discretion to employ that method. 12 U.S.C. Sec. 1823(e)

(1976) allowed FDIC to purchase assets of a failed bank only "when in the judgment of the Board of Directors such action will reduce the risk or avert a threatened loss to the Corporation [FDIC]."[1] This

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[1]Depository Insurance Flexibility Act, Sec. 113(m)(2), Pub.L. No. 97-320, 96 Stat. 1469 (1982), deleted this provision from Sec. 1823(e). The Act inserted a similar provision requiring exercise of judgment. See id. Secs. 111, 141(a)(1). That provision is codified at 12 U.S.C. Sec. 1823(c)(4)(A) (1982) and expressly limits FDIC's ability to undertake a purchase and assumption transaction unless FDIC determines that such action is "reasonably necessary to save the cost of liquidating, including paying the insured accounts" or that continued operation of the bank is necessary to provide adequate banking services to the community. Even though this amendment essentially restates, though more specifically, the old requirement for undertaking the transaction, FDIC purchased the asset in this case in 1978 under the test of 12 U.S.C. Sec. 1823(e) (1976), which is, therefore, the relevant provision for purposes of this case.

exercise of judgment requires FDIC to measure its loss under the insured deposit payoff alternative against its loss under a purchase and assumption transaction. To calculate possible loss under the purchase and assumption transaction as compared to a pay off of insured deposits, all of the failed bank's assets must be evaluated to determine the potential cost to FDIC of assuming unfavorable assets and to determine the price to be paid by the assuming bank for acceptable assets.

The process of evaluation must be undertaken quickly. "[A] purchase and assumption must be consummated with great speed, usually overnight, in order to preserve the going concern value of the failed bank and avoid an interruption in banking services." Gunter, 674 F.2d at 865. The special protections given FDIC in

Sec. 1823(e) facilitate this process by allowing FDIC to rely on the books and records of the bank in deciding whether to undertake a purchase and assumption transaction and in buying assets unacceptable to the assuming bank. An agreement not meeting the statute's requirements cannot defeat or diminish FDIC's right, title, or interest in an asset. See, e.g., Gunter; Chatham Ventures, Inc. v. FDIC, 651 F.2d 355 (5th Cir. 1981) (Unit B), cert. denied, 456 U.S. 972, 102 S.Ct. 2234, 72 L.Ed.2d 845 (1982); FDIC v. Hoover-Morris Enterprises, 642 F.2d 785 (5th Cir. 1981) (Unit B); Black v. FDIC, 640 F.2d 699 (5th Cir.) (Unit B), cert. denied, 454 U.S. 838, 102 S.Ct. 143, 70 L.Ed.2d 119 (1981). In the case at bar FDIC was entitled to rely on the books and records of WCB in deciding to undertake the

purchase and assumption transaction and in buying, in its general corporate capacity, the $84,000 participation in the Ball-Co loan.

B. MNB's theory

The court below looked solely to documents meeting the statute's requirements and excluded all of MNB's evidence tending to show WCB participated in only the unguaranteed portion but not meeting the requirements of the statute. MNB contends that before invoking Sec. 1823(e) the court was first required to isolate and define the asset in question; that is, the court had to determine whether the asset acquired by WCB was a participation in only the unguaranteed portion of the Ball-Co loan or included a ratable participation in the guaranteed

portion. And, MNB asserts, the court in isolating and defining the asset was required to consider evidence that does not meet the requirements of Sec. 1823(e), including the circumstances surrounding WCB's acquisition of the participation. This theory, that in a preliminary step the court must look to evidence not permitted by Sec. 1823(e) and then in a second step determine FDIC's rights with evidence limited by Sec. 1823(e), would destroy the effect and protection of Sec. 1823(e) in this case. MNB's construction of Sec. 1823(e) would hamper the ability of FDIC to follow the purchase and assumption alternative because uncertainty would be injected into the valuation of assets, a step crucial both in deciding to undertake the transaction and in structuring the transaction.

Section 1823(e) does not apply to every inquiry concerning an asset. It does not apply when the court determines if an asset is invalid for fraud, see Gunter, 674 F.2d at 867, or for breach of bilateral obligations contained in the asset, see Howell v. Continental Credit Corp., 655 F.2d 743, 746-48 (7th Cir. 1981) (inadequate consideration); Riverside Park Realty Co. v. FDIC, 465 F.Supp. 305, 312-13 (M.D.Tenn.1978) (breach of loan agreement). In such cases the parties contend that no asset exists or an asset is invalid and that such invalidity is caused by acts independent of any understanding or side agreement. The case before us does not fall within these narrow exceptions to Sec. 1823(e). Here MNB seeks to limit the contour of the asset as described in the certificate of participation and the

Ball-Co loan agreement that MNB furnished to WCB by asserting that an ambiguity exists in the certificate and accompanying documents. Then MNB seeks to resolve the ambiguity it created, see infra, by resorting to evidence not meeting Sec. 1823(e)'s requirements. Congress did not intend that Sec. 1823(e) be avoided in this manner; MNB's construction would drain substantial vitality from Sec. 1823(e), as applied to this case, by throwing into question the very records of the bank that the statute entitles FDIC to consider and rely upon. In the circumstances of this case, as against MNB, FDIC may rely on the books and records of WCB to establish its ratable participation in the guaranteed portion of the Ball-Co loan. We decide only this case. We leave to other forums whether under other circumstances

deficiencies in loan documents may be so patent that extrinsic evidence may be examined.

C. The district court's finding

The district court reviewed the evidence, discussed in part I, meeting the statute's requirements and concluded that WCB participated in the guaranteed portion of the Ball-Co loan. The MNB/Ball-Co loan agreement delivered to WCB with the certificate indicates that the underlying loan is protected by an 80% FmHA guarantee, and the certificate gave WCB the right to share in all collateral and security to the loan. The certificate listed collateral and security, and the list did not include the FmHA guarantee, but we hold that this MNB-created ambiguity may not be resolved by MNB through an end run around Sec.

1823(e). The minutes of the directors' meetings also indicate that the WCB's participation was guaranteed.

The trial court's finding that the Ball-Co loan was 80% guaranteed, that the books and records of the bank reflected a participation in that guaranteed loan, and that FDIC is entitled to share ratably in MNB's collection[2] on the guaranteed portion is not clearly erroneous.

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[2]The certificate requires MNB to remit to WCB "its proportionate share of collections of principal and interest when received." In the trial court MNB contended that WCB participated in only the unguaranteed portion of the Ball-Co loan and that MNB had remitted to WCB its share of collections on the 20% unguaranteed portion. On appeal MNB raises for the first time the contention that, if WCB's participation was in the guaranteed portion, MNB would nevertheless be free from liability because neither the sale of the 80% guaranteed portion of the loan to Eastern nor the payment of the guarantee by FmHA to Eastern, nor the combination of the

III. Knowledge of FDIC

MNB contends that knowledge by FDIC is relevant both to determine whether WCB participated in the guaranteed portion and to prove equitable estoppel against FDIC. We hold that knowledge of FDIC is irrelevant under either inquiry. The

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(footnote 2 continued)

two, constituted a "collection." Though not raised below, the trial court in entering judgment for FDIC implicitly found a "collection" since MNB's obligation to WCB, contained in the certificate, was to remit to WCB "its proportionate share of collections." In this posture we will not disturb that finding. See Johnson v. Smith, 696 F.2d 1334, 1338 (11th Cir. 1983) (defenses not raised and for which proof is not offered in trial court cannot be raised for the first time on appeal); Hall v. Board of School Comm'rs, 681 F.2d 965, 969-70 (5th Cir. 1982) (Unit B) (court will not consider for first time on appeal question that requires development of factual issues).

statute prescribed the requirements an agreement must meet to be valid against FDIC. If a side agreement does not meet the requirements of Sec. 1823(e), FDIC's knowledge of the terms of that side agreement does not render it valid against FDIC or estop FDIC from enforcing the agreement as contained in the failed bank's records. See FDIC v. De Jesus Velez, 678 F.2d 371, 375 (1st Cir. 1982); FDIC v. First Mortgage Investors, 485 F.Supp. 445, 451-52 (E.D.Wis.1980).

Sound policy reasons dictate against holding FDIC liable for its knowledge of side agreements as well as the hidden meaning of bank assets. In the ordinary course of business examiners from FDIC's open-bank division regularly visit all insured banks and even more frequently visit failing banks. If in undertaking a

purchase and assumption transaction FDIC's closed-bank division were held to matters of which the open-bank examiners had actual knowledge, but beyond the scope of Sec. 1823(e), the protection of Sec. 1823(e) would be lost. Any asset would be subject to challenge based on the alleged knowledge of bank examiners. The resulting uncertainty would undercut FDIC's ability to value assets quickly and precisely when conducting a purchase and assumption transaction. Cf. Gunter, 674 F.2d at 865 (discussion of speed with which transactions must be consummated to prevent halt of banking services and loss of confidence in the banking industry).

IV. Failure to extend the discovery period

The district court did not abuse its discretion in denying further discovery

concerning FDIC's knowledge of the terms of the loan participation. The discovery period had twice been extended, and evidence of FDIC's knowledge was not relevant in construing the agreement and was barred by Sec. 1823(e) if offered to validate a side agreement or to prove equitable estoppel. No showing was made that extending the discovery deadline for a third time would lead to other admissible evidence.

AFFIRMED.